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Supreme Court, U.S.
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No. 10-_____ 10-401 SEP 21 2010

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In The

Supreme Court of the United States

JEFFREY A. WEINMAN, Trustee,

Petitioner,

v.

JAMES WINSLOW GRAVES and
KATHRYN PATRICIA GRAVES,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Tenth Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Are bankruptcy debtors' contingent or illiquid interests, such as a deferred tax refund reserved to reduce a debtor's future tax liability, subject to turnover to bankruptcy trustees as property of the estate under 11 U.S.C. § 542(a)?

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

OPINIONS BELOW 1

JURISDICTION 1

STATUTORY PROVISIONS 2

STATEMENT OF THE CASE 4

REASONS FOR GRANTING THE PETITION ... 6

I. THERE IS A RECOGNIZED INTER-CIRCUIT CONFLICT REGARDING THE PROPER APPLICATION OF SECTION 542(a) TO DEFERRED TAX REFUNDS 6

II. THIS MATTER RAISES IMPORTANT ISSUES THAT MERIT THIS COURT'S REVIEW 9

CONCLUSION 14

APPENDIX

In re James Winslow Graves, No. 08-1462, Judgment (10th Cir. 2010) ..... App. 1

In re James Winslow Graves, 609 F.3d 1153 (10th Cir. 2010) ..... App. 3

In re James Winslow Graves, BAP No. CO-08-038, Judgment (Oct. 22, 2008) ..... App. 14

In re James Winslow Graves, BAP No. CO-08-038, Opinion (Oct. 22, 2008) ..... App. 16

In re James Winslow Graves, BAP No. CO-08-038, Opinion (Oct. 22, 2008) ..... App. 27

TABLE OF CONTENTS – Continued

Page

In re James and Kathryn Graves, No. 07-20569 ABC Ch. 7, Minute Order (Mar. 26, 2008) ..... App. 38

Nichols v. Birdsell, 491 F.3d 987 (9th Cir. 2007) ..... App. 40

Weinman v. Graves, No. 08-1462, Opening Br. (10th Cir. 2009) ..... App. 48

TABLE OF AUTHORITIES

Page

FEDERAL CASES

Nichols v. Birdsell, 491 F.3d 987 (9th Cir. 2007) 5, 7, 8, 9

Segal v. Rochelle, 382 U.S. 375 (1966) 6

Weinman v. Graves (In re Graves), 396 B.R. 70 (B.A.P. 10th Cir. 2008) 1, 5, 12

Weinman v. Graves (In re Graves), 609 F.3d 1153 (10th Cir. 2010) 1, 5, 6, 8, 9

FEDERAL STATUTES

11 U.S.C. § 522(d)(5) 11, 12

11 U.S.C. § 541(a) ..... *passim*

11 U.S.C. § 541(c)(1)(A) 6, 10

11 U.S.C. § 542 5

11 U.S.C. § 542(a) ..... *passim*

26 U.S.C. § 6513(d) 4

28 U.S.C. § 1254(1) 1

Bankruptcy Code, Chapter 11 ..... *passim*

RULES

Supreme Court Rule 10(a) 10

TABLE OF AUTHORITIES – Continued

Page

OTHER AUTHORITIES

4 *Collier on Bankruptcy*, ¶ 522.09 nn. 50-51 (Alan N. Resnick and Henry J. Sommer eds., 16th ed. 2010) 12

G *Collier on Bankruptcy*, app. pt. 44-11, 44-12 (Alan N. Resnick and Henry J. Sommer eds., 15th ed. revised 2007) 11

Administrative Office of the U.S. Courts, Bankruptcy Filings Up 20 Percent in June (Aug. 17, 2010), http://www.uscourts.gov/News/NewsView/10-08-17/Bankruptcy_Filings_Up_20_Percent_in_June.aspx?CntPageID=1 13

PETITION FOR A WRIT OF CERTIORARI

Petitioner and bankruptcy trustee Jeffrey A. Weinman ("the Trustee") respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Tenth Circuit in this case.

OPINIONS BELOW

The bankruptcy court's unpublished minute order denying the Trustee's motion for turnover is reproduced in the appendix ("App.") at App. 38-39. The bankruptcy court's oral comments on the record are reproduced at App. 16-26. The Bankruptcy Appellate Panel of the Tenth Circuit Court of Appeals' opinion is published at 396 B.R. 70 (B.A.P. 10th Cir. 2008), and is reproduced at App. 27-37. The Tenth Circuit's opinion is published at 609 F.3d 1153 (10th Cir. 2010), and is reproduced at App. 3-13.

JURISDICTION

The Tenth Circuit filed its decision on June 29, 2010. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS

1. Section 541(a)[1] provides:

> The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
>
> (1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.
>
> (2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is –
>
> (A) under the sole, equal, or joint management and control of the debtor; or
>
> (B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.
>
> (3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

---

[1] Unless expressly indicated otherwise, all "Section" references are to the Bankruptcy Code, Chapter 11 of the United States Code.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date –

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

11 U.S.C. § 541(a).

2. Section 542(a) provides:

> Except as provided in subsection (c) or (d) of this section, an entity, other than a custodian, in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease under section 363 of this title, or that the debtor may exempt under section 522 of this title, shall deliver to the trustee, and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate.

11 U.S.C. § 542(a).

STATEMENT OF THE CASE

Debtors James Winslow Graves and Kathryn Patricia Graves ("the Debtors") filed a 2006 federal tax return in July 2007. They were entitled to a $3,000 tax refund. Instead of taking the overpayment as a refund, the Debtors elected to apply that refund as a dollar-for-dollar credit to future taxes owed. Such an election is irrevocable during the subsequent tax year. 26 U.S.C. § 6513(d) ("[N]o claim for credit or refund of such overpayment shall be allowed for the taxable year in which the overpayment arises.").

On September 20, 2007, just weeks after they elected to defer their tax refund, the Debtors filed a voluntary Chapter 7 bankruptcy petition with the United States Bankruptcy Court for the District of

Colorado. The Trustee moved to compel the Debtors to turn over their interest in the credit as property of the estate under Section 541(a). The bankruptcy court denied the motion, ruling that the Debtors were not in possession of the credit and could not be compelled to turn it over under Section 541(a).

The Trustee timely appealed to the United States Bankruptcy Appellate Panel ("BAP") for the Tenth Circuit. The BAP correctly noted that "[t]he single issue presented by this appeal is whether a pre-petition tax refund that the Debtors elected to apply in pre-payment of a subsequent year's tax liability is properly subject to turnover pursuant to 11 U.S.C. § 542." *Weinman v. Graves (In re Graves)*, 396 B.R. 70, 72 (B.A.P. 10th Cir. 2008). The BAP affirmed the bankruptcy court's prior ruling, holding that "[a] contingent right to a refund . . . is not something, in our opinion, that is subject to turnover." *Id.* at 75.

The Trustee timely filed a notice of appeal to the Tenth Circuit Court of Appeals on November 21, 2008. The Tenth Circuit affirmed. The court recognized "that, to a large extent, this holding conflicts with the Ninth Circuit's decision in *Nichols* . . . that the entire refund amount was property of the estate and implicitly subject to turnover from the debtors." *Weinman v. Graves (In re Graves)*, 609 F.3d 1153, 1158 (10th Cir. 2010) (*citing Nichols v. Birdsell*, 491 F.3d 987 (9th Cir. 2007)). It nevertheless held "that only the part of the refund that (1) is attributable to pre-petition earnings and (2) reverted to debtors after

application of the refund to their ultimate (2007) tax liability, is subject to turnover." *Id.* at 1159.

REASONS FOR GRANTING THE PETITION

I. THERE IS A RECOGNIZED INTER-CIRCUIT CONFLICT REGARDING THE PROPER APPLICATION OF SECTION 542(a) TO DEFERRED TAX REFUNDS.

At issue in this case is whether, under Section 542(a), a trustee may compel a debtor to turn over the value of a pre-petition tax refund that was deferred as a credit against post-petition tax obligations. As described below, the Ninth and Tenth Circuits have reached conflicting conclusions in deciding this issue, thus satisfying the "conflict" prong of Supreme Court Rule 10(a).

By way of background, Section 541(a) broadly defines "property" of a bankruptcy estate to include "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a). An interest is property even if transfer or use of that interest is restricted at the time the bankruptcy petition is filed. 11 U.S.C. § 541(c)(1)(A) (interest is property of estate under Section 541(a) even if it is subject to nonbankruptcy law "that restricts or conditions transfer of such interest by the debtor"); *Segal v. Rochelle*, 382 U.S. 375, 379 (1966) ("[T]he term 'property' has been construed most generously and an interest is not outside its reach

because it is novel or contingent or because enjoyment must be postponed.").

Section 542(a), in turn, provides that a trustee may compel a debtor who is in "possession, custody, or control" of any estate property to turn over such property if it is property that the trustee may use, sell, or lease under Section 363. 11 U.S.C. § 542(a). That section also allows the trustee to compel the turnover of "*the value of such property*" in lieu of the property itself. *Id.* (emphasis added). Accordingly, under Section 542(a), a debtor can be compelled to turn over to the trustee that property or the value of such property in lieu of the property itself.

The question presented by this Petition is whether a debtor may be compelled under Section 542(a) to turn over to the trustee the total value of a pre-petition tax refund that the debtor irrevocably deferred and left on deposit with the IRS as a prepaid credit against post-petition tax liability. The Ninth and Tenth Circuits have reached conflicting results on this issue. As noted above, the Ninth Circuit addressed this issue in *Nichols*. The debtors there overpaid their 2001 state and federal taxes and elected to leave the overpayment on file as a credit against future taxes. *Nichols*, 491 F.3d at 988. The trustee moved to compel turnover of that property interest under Section 542(a). The Ninth Circuit expressly recognized that the credit was property of the estate, that the debtors held the credit, and that Section 542(a) required them to turn it over. The court explained:

> As a result of the election, the Debtors were left with a credit with the IRS that provided a dollar-for-dollar tax reduction in the following year. If the [Debtors] had not elected to prepay their taxes, those funds would have been refunded to them and would likely have been available for the bankruptcy estate when they voluntarily filed for bankruptcy just 16 days later. The fact that the election, once made, was irrevocable, does not change the analysis. In light of the expansive definition of property contained in the Bankruptcy Code . . . we hold that this credit toward future taxes constituted estate property at the time the Debtors filed for bankruptcy.

Id. at 990. The court therefore directed the debtors to turn over the value of the credit to the estate. *Id.* at 988.

In this case, the Tenth Circuit reached a conflicting result and in so doing expressly acknowledged the resulting inter-circuit conflict. Addressing the same issue that the Ninth Circuit addressed in *Nichols*, the Tenth Circuit squarely held "that only the part of the refund that (1) is attributable to pre-petition earnings and (2) reverted to debtors after application of the refund to their ultimate (2007) tax liability, is subject to turnover." *Graves*, 609 F.3d at 1159. Thus, in the Ninth Circuit, the *entirety* of such tax credits is property of the estate subject to turnover under Section 542(a) while in the Tenth Circuit only a *portion* of such credits – if any – is property subject to turnover under the same statutory provisions.

In so holding, the Tenth Circuit expressly acknowledged the resulting inter-circuit conflict. Addressing that issue, the Tenth Circuit stated:

> We are aware that, to a large extent, this holding conflicts with the Ninth Circuit's decision in *Nichols*, 491 F.3d 987. There, in a case factually indistinguishable from this one, the Ninth Circuit held that the entire refund amount was property of the estate and implicitly subject to turnover from the debtors.

Id. at 1158. The Tenth Circuit further noted:

> We find some appeal in the reasoning of the Ninth Circuit that, by electing to have their 2006 refund applied to 2007 taxes, the debtors in *Nichols*, like debtors here, received something of value, i.e., a dollar-for-dollar reduction on their 2007 taxes, money that could have been available to the bankruptcy estate had the election not been made.

Id. at 1158-59. The Tenth Circuit nevertheless declined to hold that this same property interest is subject to turnover under Section 542(a), thus creating an inter-circuit conflict.

II. THIS MATTER RAISES IMPORTANT ISSUES THAT MERIT THIS COURT'S REVIEW.

As set forth above, there is a clear and acknowledged inter-circuit conflict regarding the proper

application of Section 542(a) to deferred tax refunds, thus satisfying the "conflict" prong of Supreme Court Rule 10(a). The matter also raises important questions of federal law, which similarly merit this Court's review.

As an initial matter, the Tenth Circuit logic – if permitted to stand – would apply well beyond deferred tax refunds to other types of contingent reversionary interests. The Tenth Circuit erroneously held that a contingent or illiquid property interest cannot be in the "possession, custody, or control" of a debtor. That conclusion is contrary to the Bankruptcy Code's definition of "property," which explicitly states that a debtor's property may include such interests. 11 U.S.C. §§ 541(a), 541(c)(1)(A). The Code also provides a specific solution for how to treat property that is nontransferable: Section 542(a) authorizes the trustee to compel turnover of "*the value of such property*" in lieu of the property itself. 11 U.S.C. § 542(a) (emphasis added). Thus, contrary to the Tenth Circuit's holding, the plain language of Section 542(a) does not allow courts to exempt (or otherwise protect from creditors) property that is contingent or illiquid in nature.

If such an exception were to exist, the consequences would be profound. It would allow a debtor to shield from creditors any interests that are nontransferable and contingent or illiquid in nature. There are, in addition to deferred tax refunds, many such interests, including prepaid health savings accounts, prepaid rent, a spouse's dower interest, and prepaid

entertainment costs such as gym memberships. Under the Tenth Circuit's analysis – unlike the Ninth Circuit's analysis – such contingent and/or illiquid interests are not subject to turnover under Section 542(a) as Congress clearly intended.

The Tenth Circuit's opinion also undermines Congressional intent as reflected in the Bankruptcy Code, which was intended to strike a delicate balance between the interests of debtors in obtaining a fresh start and the interests of creditors in repayment of debts. G *Collier on Bankruptcy*, app. pt. 44-11, 44-12 (Alan N. Resnick and Henry J. Sommer eds., 15th ed. revised 2007) ("Balance is essential. Without it, the American bankruptcy system can be neither equitable nor efficient. The laws enacted over the last 100 years have had balance as their goal and their common theme, spoken or unspoken, trying to provide both fair treatment for creditors and a fresh start for debtors."). Congress carefully delineated this delicate balance of competing interests in the Bankruptcy Code.

A key element of that careful balance is the debtor's ability to exempt property from the reach of the bankruptcy estate. That exemption, codified in Section 522, allows a debtor to exempt various items of property. It includes a catch-all provision, codified in Section 522(d)(5), which allows a debtor to exempt a specified amount of "any property" the debtor chooses – assuming the debtor has not spent that

exemption on other items. 11 U.S.C. § 522(d)(5).[2] As this statutory provision shows, Congress carefully and specifically limited the amount of property that debtors can exempt in order to ensure that creditors would not be deprived of more property than necessary to allow debtors a fresh start.

The Tenth Circuit's decision upsets that balance by, in effect, allowing debtors to exempt *more* than the amounts Congress allowed if they utilize pre-petition earnings to acquire tax credits or otherwise prepay expenses. The decision effectively eviscerates Section 542 by allowing debtors to unilaterally protect estate property from turnover. Stated another way, it allows debtors to enjoy the value of pre-petition income – property that is part of the estate and can be used to protect creditors' interests – as though such income were actually earned post-petition and therefore protected by the fresh-start principle.

It is equally clear that this case is an appropriate vehicle to review the issue presented. As the BAP in this matter correctly noted, the dispositive issue is purely legal in nature. *Graves*, 396 B.R. at 72 (quoted on page 5 above). Over time, lower courts will presumably follow the Tenth Circuit's analysis – to the

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[2] $11,000 was the total amount of exemption allowed for cases filed from April 1, 2007 to April 1, 2010. 4 *Collier on Bankruptcy*, ¶ 522.09 nn. 50-51 (Alan N. Resnick and Henry J. Sommer eds., 16th ed. 2010).

detriment of the bankruptcy estate and creditors – or follow the Ninth Circuit's analysis – thus widening the inter-circuit conflict. This Court can, and should, accept review so that it can correct the resulting imbalance and resolve the existing inter-circuit conflict *before* creditors are improperly deprived of important assets that should properly be available for payment of debts.

Indeed, prompt resolution of the existing inter-circuit conflict is especially important given the dramatic rise in bankruptcy filings following the 2008 financial crisis and ensuing economic recession. According to statistics compiled by the Administrative Office of the U.S. Courts, nearly 1.6 million bankruptcies were filed during the year ending June 30, 2010: a 20 percent increase over the previous year and "the highest number of bankruptcy filings for any period since many of the provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 took effect."[3] The issue presented by this Petition may arise in many of those matters, which are currently pending in courts across the country. By accepting review at this time, the Court can clarify the law regarding turnover of contingent or illiquid interests under Section 542(a) – including but not limited to turnover of deferred tax refunds reserved

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[3] Administrative Office of the U.S. Courts, Bankruptcy Filings Up 20 Percent in June (Aug. 17, 2010), http://www.uscourts.gov/News/NewsView/10-08-17/Bankruptcy_Filings_Up_20_Percent_in_June.aspx?CntPageID=1.

to reduce a debtor's future tax liability – and prevent the inconsistent rulings that are likely to result from the existing inter-circuit conflict.

CONCLUSION

For each of these reasons, this Court should grant a writ of certiorari to review the judgment and opinion of the Tenth Circuit.

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

In Re: JAMES WINSLOW GRAVES, d/b/a Custom Woods Construction, LLC, and KATHRYN PATRICIA GRAVES, Debtors,	
JEFFREY A. WEINMAN, Trustee, Appellant, v. JAMES WINSLOW GRAVES; KATHRYN PATRICIA GRAVES, Appellees.	No. 08-1462 (BAP No. 08-038-CO)

JUDGMENT

(Filed June 29, 2010)

Before **BRISCOE**, Chief Judge, **HOLLOWAY**, and **EBEL**, Circuit Judges.

This case originated from the Tenth Circuit Bankruptcy Appellate Panel and was submitted on the briefs at the direction of the court.

The judgment of that court is affirmed.

Entered for the Court,

/s/ Elisabeth A. Shumaker
ELISABETH A. SHUMAKER,
Clerk

In re: JAMES WINSLOW GRAVES, d/b/a Custom Woods Construction, LLC, and KATHRYN PATRICIA GRAVES, Debtors. JEFFREY A. WEINMAN, Trustee, Appellant, v. JAMES WINSLOW GRAVES; KATHRYN PATRICIA GRAVES, Appellees.

No. 08-1462

UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

609 F.3d 1153*; *2010 U.S. App. LEXIS 13249*; *2010-2 U.S. Tax Cas. (CCH) P50,499*; *106 A.F.T.R.2d (RIA) 5050*; *Bankr. L. Rep. (CCH) P81,799

June 29, 2010, Filed

COUNSEL: Submitted on the briefs: *

Jeffrey A. Weinman, Appellant, Pro se.

JUDGES: Before BRISCOE, Chief Judge, HOLLOWAY, and EBEL, Circuit Judges.

OPINION BY: HOLLOWAY

OPINION

HOLLOWAY, Circuit Judge.

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* After examining the briefs and appellate record, this panel has determined unanimously that oral argument would not materially assist the determination of this appeal. *See* Fed. R. App. P. 34(a)(2); 10th Cir. R. 34.1(G). The case is therefore ordered submitted without oral argument.

The issue in this case is narrow: is debtors' interest in a 2006 tax refund, irrevocably applied pre-petition to 2007 taxes, subject to turnover under 11 U.S.C. § 542(a)? The Bankruptcy Appellate Panel (BAP) for this Circuit answered in the negative. We hold that only the amount of any subsequent refund of 2007 taxes attributable to pre-petition earnings is subject to turnover, and we affirm with modification.

In July 2007, prior to becoming Chapter 7 debtors, James and Kathryn Graves filed their 2006 tax return. Pursuant to that return, the Graveses were entitled to a $ 3000.00 tax refund. Instead of choosing to receive a current refund of that money from the IRS, the Graveses elected to leave those funds on deposit with the United States and apply the overpayment to their future tax liability. This election is irrevocable. Where an overpayment of tax is applied as a credit on the next year's taxes, "no claim for credit or refund of such overpayment shall be allowed for the taxable year in which the overpayment arises." 26 U.S.C. § 6513(d). Two months after filing their tax return, the Graveses filed for bankruptcy protection.

Jeffrey A. Weinman, appellant and trustee of the bankruptcy estate ("trustee"), filed a motion for turnover of debtors' 2006 tax refund under 11 U.S.C. § 542(a). 11 U.S.C. § 542(a) provides in relevant part that:

> an entity, other than a custodian, in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease under section 363 of this title, or that the debtor may exempt under section 522 of this title, shall deliver to the trustee, and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate.

In his motion, the trustee argued that the refund amount was property of the estate under 11 U.S.C. § 541(a)(1), and that, since debtors were receiving the benefit of the application of the refund, the funds should be treated as an account receivable of the debtors, and debtors should therefore be required to turn over an equivalent amount to the estate. The bankruptcy court denied the trustee's motion, and the BAP affirmed. *Weinman v. Graves (In re Graves)*, 396 B.R. 70 (B.A.P. 10th Cir. 2008). The trustee filed a timely notice of appeal, triggering our jurisdiction over the appeal under 28 U.S.C. § 158(d)(1).

In agreeing with the bankruptcy court that debtors could not be ordered to turn over that which they did not have, i.e., "the amount they could have received from the IRS in 2007, but did not," *In re Graves*, 396 B.R. at 73, the BAP assumed, without deciding, that debtors' "pre-payment constitutes estate property as a contingent reversionary interest." *Id.* at 75. The BAP further concluded, however, that the Bankruptcy Code's turnover provision, 11 U.S.C. § 542, does not empower a trustee to demand

turnover from a debtor under these circumstances. *Id.* In doing so the BAP noted that, because of 26 U.S.C. § 6513(d), debtors "had no current right to possession of the pre-paid taxes" at the time they filed their petition or at the time the trustee filed the turnover action. *Id.* Since the debtors' interest in the overpayment was limited at the time of the petition, the trustee's right to possession was similarly limited. *Id.* The BAP concluded that "[a] contingent right to a refund in the event that the Debtors overpaid their 2007 taxes is not something, in our opinion, that is subject to turnover." *Id.*

"We review the BAP's decision *de novo* because [t]here are no factual disputes and the issues on appeal pertain to the proper application of bankruptcy statutes and interpretation of case law. . . . In this review, we independently review the Bankruptcy Court's decision." *Zubrod v. Duncan (In re Duncan)*, 329 F.3d 1195, 1198 (10th Cir. 2003) (quotation and citations omitted).

The bankruptcy estate is comprised of "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). The statute is deliberately broad in scope. *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 204-05, 103 S. Ct. 2309, 76 L. Ed. 2d 515 (1983). Estate property does not have to be "immediately capable of being liquidated into cash in order to constitute property of the estate," and includes debtor's interests which "cannot be liquidated and transferred by

the debtor." *Nichols v. Birdsell*, 491 F.3d 987, 990 (9th Cir. 2007).

One of the central precepts of bankruptcy law is that

> a bankruptcy trustee succeeds only to the title and rights in property that the debtor had at the time she filed the bankruptcy petition. Filing a bankruptcy petition does not expand or change a debtor's interest in an asset; it merely changes the party who holds that interest. Further, a trustee takes the property subject to the same restrictions that existed at the commencement of the case. To the extent an interest is limited in the hands of a debtor, it is equally limited as property of the estate.

In re Sanders, 969 F.2d 591, 593 (7th Cir. 1992) (citations and quotations omitted); *see also* Collier on Bankruptcy P 541.01 at 541-8.3 (15th ed. rev. 2009) ("Subdivision (d) of [§ 541] makes clear that the estate can only succeed to the same property interest that the debtor possesses, and cannot achieve a greater interest.").

Applying this principle, it is clear that the trustee's interest in the application of the tax refund must be limited to the same extent as the debtors' interest – here by the strictures of 26 U.S.C. § 6513(d), which makes debtors' refund-application election irrevocable. Debtors will have no right to any cash from the $ 3000 refund applied as a prepayment of their 2007

taxes until after their 2007 tax liability is determined, and then only if they are entitled to a further refund. The portion of that further refund attributable to pre-petition earnings would become property of the estate. Thus, we hold that the estate's interest in the pre-payment is limited to debtors' contingent reversionary interest in the pre-payment attributable to pre-petition earnings. *See In re Middendorf*, 381 B.R. 774, 778-80 (Bankr. D. Kan. 2008) ("The debtors' interest in a pre-petition tax overpayment is a contingent reversionary interest pending the final determination of the debtors' tax liability. Once the ultimate tax liability is assessed and satisfied, the debtors' interest vests in the resulting refund attributable to pre-petition funds."); *cf. Redmond v. Lentz & Clark, P.A. (In re Wagers)*, 514 F.3d 1021, 1029, 355 B.R. 268 (10th Cir. 2007) (recognizing that "even a contingent, reversionary interest is included in a debtor's estate under § 541").[1]

Turning to whether turnover is appropriate under these circumstances, we first consider the

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[1] We acknowledge a line of authority holding that an applied tax refund is not estate property. *See United States v. Pritchard (In re Block)*, 141 B.R. 609, 611 (N.D. Tex. 1992) (holding that monies were not property of the estate once the irrevocable election had been made and thus were not subject to turnover); *Grant v. United States (In re Simmons)*, 124 B.R. 606, 607-08 (Bankr. M.D. Fla. 1991) (same). Given that some part of an applied refund may be available after the ultimate tax liability is determined and that part of that amount may be attributable to pre-petition earnings, we think a more comprehensive result is as expressed herein.

statutory language which requires that the turnover target, here debtors, be "in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease under [11 U.S.C. §] 363." 11 U.S.C. § 542(a). We agree with the BAP that, after filing their Chapter 7 petition and at least through the culmination of the turnover proceeding, debtors were never in "possession, custody, or control" of their contingent reversionary interest in the prepayment of their 2007 taxes. *See Maggio v. Zeitz (In re Luma Camera Serv., Inc.)*, 333 U.S. 56, 64, 68 S. Ct. 401, 92 L. Ed. 476 (1948) (holding that "the primary condition of [turnover] relief is possession of existing chattels or their proceeds capable of being surrendered by the person ordered to do so").[2] This fact alone dooms the trustee's efforts.[3]

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[2] Debtors presumably controlled the refund before they made their election to apply it to future taxes, but that control was pre-petition and thus not "during the case" as required by § 542(a).

[3] The fact that debtors had never been in possession of the refund or the prepayment during the case makes it unnecessary for us to engage in the debate about whether § 542(a) requires them to turn over the "value" of the refund, given the statutory language requiring a turnover target to deliver to the trustee "property or the value of such property." The cases relying on the "value of such property" language involve turnover targets who, at least some time during the case, possessed the debtor's funds. *See, e.g., Beaman v. Vandeventer Black, LLP (In re Shearin)*, 224 F.3d 353, 356 (4th Cir. 2000) (law firm, having possessed year-end profits of debtor/partner during the case, forced to turnover equivalent amount to trustee despite no longer having possession of the funds at the time of the turnover proceeding); *Boyer*

(Continued on following page)

Resort to § 542 cannot be used to broaden the trustee's interest in the refund, the pre-payment of 2007 taxes or in any other estate property. *United States v. Neary* (*In re Armstrong*), 206 F.3d 465, 472 (5th Cir. 2000); *French v. Johnson* (*In re Coomer*), 375 B.R. 800, 806 (Bankr. N.D. Ohio 2007). In *In re Armstrong*, the Fifth Circuit held that § 542(a) cannot be used to avoid the statute of limitations inherent in 26 U.S.C. § 6511, the general tax-refund statute. The Fifth Circuit noted that "[b]ecause that right [to a refund] is created and circumscribed by § 6511 and nothing explicitly changes its terms, § 542(a) cannot be read to expand the right to file for a refund to give the trustee unlimited time so long as the bankruptcy continues," *id.* at 472. Further, "[b]ecause the debtor does not have a continuing interest in the tax overpayment under § 541(a)(1), other than that created by § 6511, *the trustee cannot use § 542(a) to create interests not otherwise in existence*." *Id.* at n.6 (emphasis added).

Similarly, in *French v. Johnson*, the trustee attempted to secure turnover of the debtor's interest

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v. Carlton, Fields, Ward, Emmanuel, Smith & Cutler, P.A. (In re USA Diversified Prods., Inc.), 100 F.3d 53, 55-56 (7th Cir. 1996) (same, with law firm that possessed funds of debtor which it erroneously returned to debtor's president and noting that § 542 requires delivery of property or the value of the property); *Bailey v. Suhar* (*In re Bailey*), 380 B.R. 486, 493 (B.A.P. 6th Cir. 2008) (requiring debtors to turn funds over to the trustee equal to the amount of the tax refund they obtained post-petition and transferred to their attorney).

in a residential security deposit. In rejecting the trustee's contention that § 542(a) gave him a substantive right to the deposit, the court stated:

> Section 542(a) is best viewed as an enabling provision, allowing the trustee to obtain possession of property only where the debtor otherwise had a *right to possess* the property. But where a debtor, and thus the trustee, does not have a right *to possess or use* property at the commencement of the case, the right generally cannot be acquired through a turnover action under § 542(a). That is, a bankruptcy trustee may not compel the turnover of property pursuant to § 542(a) if the debtor had no right to obtain the property.

Id. (citation omitted). Because, at no time during the case up to the filing of the turnover action, did debtors have the right to obtain their refund or prepayment from the IRS, the trustee could not compel turnover of that amount, and the bankruptcy court correctly denied the turnover motion.

Things may be different now, however, because it is likely that debtors' 2007 tax liability has been determined. If debtors were entitled to a refund after their 2007 tax liability was satisfied, the trustee is entitled to demand turnover of any amount of such refund attributable to pre-petition earnings. *See In re Middendorf*, 381 B.R. at 778-80; *Traina v. Orrill* (*In re Orrill*), 226 B.R. 563 (Bankr. E.D. La. 1997).

In addition to the statutory basis underpinning our conclusion, we are also of the opinion that, from policy and practicality standpoints, this is the proper solution. A turnover order issued at the time the trustee requested it here would have required debtors to expend post-petition earnings or exempt assets in order to comply with the order. *See In re Blagg*, 372 B.R. 502, 510 (Bankr. D. Kan. 2007). Such an outcome would have contravened the spirit of the bankruptcy laws which aim to create a fresh start for Chapter 7 debtors. *Id.* Further, from a practical standpoint, we agree with the bankruptcy judge who determined that a turnover order under these circumstances would simply result in a contempt procedure where the defense would most likely be impossibility [sic], all resulting in a waste of the court's time. Aplt. App. at 40.

We are aware that, to a large extent, this holding conflicts with the Ninth Circuit's decision in *Nichols*, 491 F.3d 987. There, in a case factually indistinguishable from this one, the Ninth Circuit held that the entire refund amount was property of the estate and implicitly subject to turnover from the debtors. In doing so, however, the court focused entirely on whether the refund was property of the estate and neither discussed turnover nor analyzed the case in light of the language of § 542(a). It is therefore unclear how the Ninth Circuit would apply the statutory requirements for turnover, which clearly require possession during the case, to the present situation.

We find some appeal in the reasoning of the Ninth Circuit that, by electing to have their 2006 refund applied to 2007 taxes, the debtors in *Nichols*, like debtors here, received something of value, i.e, a dollar-for-dollar reduction on their 2007 taxes, money that could have been available to the bankruptcy estate had the election not been made. The fact that all or part of a tax prepayment can be estate property, however, does not determine the extent of the property interest in the hands of the trustee nor, as discussed above, does it determine whether that interest is subject to turnover.

In summary, we hold that the pre-petition portion of the refund is property of the estate. We go further, however, to hold that only the part of the refund that (1) is attributable to pre-petition earnings and (2) reverted to debtors after application of the refund to their ultimate (2007) tax liability, is subject to turnover.

With the modifications discussed above, the judgment of the Bankruptcy Appellate Panel is AFFIRMED.

UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE TENTH CIRCUIT

IN RE JAMES WINSLOW GRAVES, doing business as Custom Woods Construction, LLC, and KATHRYN PATRICIA GRAVES, Debtors. JEFFREY A. WEINMAN, Trustee, Appellant, v. JAMES WINSLOW GRAVES and KATHRYN PATRICIA GRAVES, Appellees.	BAP No. CO-08-038 Bankr. No. 07-20569-ABC Chapter 7

JUDGMENT
Filed October 22, 2008

Before BOHANON, MICHAEL, and THURMAN, Bankruptcy Judges.

The judgment of this Court has entered in accordance with the Published Opinion issued on October 22, 2008.

For the Panel:
Barbara A. Schermerhorn,
Clerk of Court

By: /s/ Kelly Hopfer
Kelly Hopfer
Attorney Deputy Clerk

PUBLISH

UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE TENTH CIRCUIT

IN RE JAMES WINSLOW GRAVES, doing business as Custom Woods Construction, LLC, and KATHRYN PATRICIA GRAVES, Debtors.	BAP No. CO-08-038 Bankr. No. 07-20569-ABC Chapter 7 OPINION
JEFFREY A. WEINMAN, Trustee, Appellant, v. JAMES WINSLOW GRAVES and KATHRYN PATRICIA GRAVES, Appellees.	(Filed Oct. 22, 2008)

Appeal from the United States Bankruptcy Court for the District of Colorado

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Submitted on the briefs:*

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* The parties did not request oral argument, and after examining the briefs and appellate record, the Court has determined unanimously that oral argument would not materially

(Continued on following page)

Jeffrey A. Weinman, Trustee, pro se.

Before BOHANON, MICHAEL, and THURMAN, Bankruptcy Judges.

THURMAN, Bankruptcy Judge.

The Chapter 7 bankruptcy trustee appeals the bankruptcy court's order denying his motion to compel debtors, James and Kathryn Graves ("Debtors") to turnover the value of a pre-petition tax refund that Debtors applied to pre-payment of their 2007 taxes, prior to filing their bankruptcy case. We affirm.

I. BACKGROUND

In July 2007, Debtors filed their 2006 tax return. Pursuant to that return, Debtors were entitled to a refund for overpayment of taxes in the amount of $3,000.[1] The Debtors filed a voluntary Chapter 7 bankruptcy petition on September 20, 2007, and did

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assist in the determination of this appeal. *See* Fed. R. Bankr. P. 8012. The case is therefore ordered submitted without oral argument.

[1] Although the Debtors' tax return directs that the amount of $3,820 be applied to their 2007 estimated tax, this is because they failed to subtract the amount of taxes owed for 2006, $820, from the amount of taxes paid in 2006, $3,820. *See Debtors' IRS 1040 (2006)* at 2, *in* Appellants' Amended Appendix at 19. Thus, their actual refund entitlement was only $3,000, and that is the amount for which they received a pre-payment credit.

not elect to split their tax year pursuant to 26 U.S.C. § 1398(d)(2).[2] In January 2008, trustee Jeffrey Weinman ("Trustee"), filed a motion for turnover of the Debtors' 2006 tax refund. The Debtors responded, and the matter was considered at a non-evidentiary hearing on March 26, 2008. The bankruptcy court ruled orally on the record and, on the same date, issued a minute entry denying the Trustee's motion. The Trustee filed a notice of appeal on April 4, 2008 and, on June 3, 2008, this Court issued an order determining the minute entry to be a final order for the purposes of appeal.

II. APPELLATE JURISDICTION

This Court has jurisdiction to hear timely-filed appeals from final judgments and orders of bankruptcy courts within the Tenth Circuit, unless one of the parties elects to have the district court hear the appeal.[3] Because this Court has already determined that the order sought to be appealed is final, the notice of appeal was timely filed, and no party to this appeal has elected to have the appeal heard by the district court, this Court has appellate jurisdiction.

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[2] This provision allows debtors in Chapter 7 and 11 cases to treat their taxable year as two taxable years; one ending on the day prior to filing of their petition, and the other beginning on the petition date. However, any such election must be made on or prior to the date on which the bankruptcy case is commenced.

[3] 328 U.S.C. § 158(a)(1), (b)(1), and (c)(1); Fed. R. Bankr. P. 8002.

III. ISSUE AND STANDARD OF REVIEW

The single issue presented by this appeal is whether a pre-petition tax refund that the Debtors elected to apply in pre-payment of a subsequent year's tax liability is properly subject to turnover pursuant to 11 U.S.C. § 542. This is an issue of law, which this Court reviews *de novo*.[4]

IV. DISCUSSION

This appeal exemplifies the concept that "you cannot get blood out of a turnip." The Trustee seeks to obtain from the Debtors that which they simply do not have: the amount they could have received from the IRS in 2007, but did not. In most lawsuits or contested matters, plaintiffs or others obtain judgments or orders for damages without consideration of the defendants' ability to pay. However, this is not an ordinary matter, but a Chapter 7 bankruptcy case, which is governed by the Bankruptcy Code. Thus, in this case, a trustee has been appointed to, among other duties, "collect and reduce to money the property of the estate."[5] In order to carry out their duties, bankruptcy trustees are given certain powers by the Bankruptcy Code. Section 542(a) of the Bankruptcy Code authorizes a bankruptcy trustee to compel turnover of estate property from anyone who has it in their "possession, custody, or control, during the

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[4] *In re Duncan*, 329 F.3d 1195, 1198 (10th Cir. 2003).

[5] 11 U.S.C. § 704(a).

case."[6] The Trustee contends that the Debtors' 2006 tax refund is both property of the estate and subject to the turnover power. The Debtors respond that, because of their pre-payment election, they are not now, and never have been, in possession, custody, or control of that refund during the pendency of the bankruptcy case.

This is not the first case involving such a dispute. Several of these cases deserve our analysis. In 1948, the United States Supreme Court defined the pre-Bankruptcy Code turnover power, noting that "the primary condition of [turnover] relief is possession of existing chattels or their proceeds capable of being surrendered by the person ordered to do so."[7] The Court also noted that "we do not consider resort to this particular proceeding [turnover] appropriate if, at the time it is instituted, the property and its proceeds have already been dissipated, no matter when that dissipation occurred."[8] These concepts were subsequently incorporated into the statutory turnover provision, § 542(a).

In *Grant v. United States (In re Simmons)*,[9] the debtor elected to have an overpayment of taxes applied to his next year's tax liability. Six days later, he

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[6] 11 U.S.C. § 542(a).

[7] *Maggio v. Zeitz (In re Luma Camera Serv., Inc.)*, 333 U.S. 56, 64 (1948).

[8] *Id.* at 64.

[9] 124 B.R. 606 (Bankr. M.D. Fla. 1991).

filed for Chapter 7 bankruptcy relief. The trustee in bankruptcy filed an adversary proceeding against the Internal Revenue Service ("IRS") seeking turnover of the prepaid funds. The court denied the relief, finding that the prepaid funds were not property of the estate, stating:

> Thus, debtor's overpayment, at his election, became a payment of his 1988 estimated tax rather than an overpayment of his 1987 taxes. Once debtor made this election, as a matter of law, he no longer had an overpayment for which he could file a claim for refund. Consequently, the debtor's prepetition estimated tax payment cannot be considered a legal or equitable interest of the debtor in property as of the commencement of the case, and such payment is not subject to turnover.

Id., at 607-08. This outcome was based, in part, on the Internal Revenue Code, 26 U.S.C. § 6513(d), which provides that, where an overpayment of tax is applied as a credit on the next year's taxes, "no claim for refund of such overpayment shall be allowed for the taxable year in which the overpayment arises."

The trustee in *Wittman v. United States (In re Weir)*,[10] similarly attempted to obtain prepaid taxes from the IRS, asserting claims for turnover, voidable preference, and fraudulent conveyance. The court rejected all three claims. With respect to the turnover

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[10] No. 85-40456-7, 1990 WL 63072 (Bankr. D. Kan. Apr. 3, 1990).

claim, the court noted that, once the prepayment election had been made, "debtor retained only the right to have the payment credited against his 1985 tax liability and to have any excess refunded to him."[11] However, the court did note that, although the estate was not entitled to recover the prepayments as property of the estate, it "would be entitled to share in any refund due the debtor."[12]

In *In re Middendorf*,[13] debtors pre-paid $22,250 on their 2005 taxes, eight days before filing a Chapter 7 petition. In 2006, debtors filed their 2005 tax return, which entitled them to a refund in excess of $20,000. The trustee made demand on the IRS for the entire pre-payment amount, contending that it was a preferential transfer. Trustee and the IRS entered a settlement, subject to the court's approval, for turnover of the entire pre-payment amount. Debtors objected. The court found that the debtors' pre-payment did not constitute a preference, because a preference requires proof of payment of an antecedent debt. Since debtors' 2005 tax obligation did not arise until the end of 2005, and the pre-payment occurred in April 2005, the trustee could not prove that element of the claim. Likewise, the court held that the pre-payment was not a fraudulent transfer because debtors had received reasonably equivalent value for

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[11] *Id.* at *2.

[12] *Id.*

[13] 381 B.R. 774 (Bankr. D. Kan. 2008).

the payment, which consisted of a dollar for dollar credit and the right to a refund if their next year's tax debt was less than the pre-payment. Nonetheless, the court held that "the portion of Debtors' tax refund attributable to pre-petition withholdings and payments is Estate property," and that the debtors' "contingent reversionary interest" vests "once the ultimate tax liability is assessed and satisfied."[14]

Finally, the Ninth Circuit Court of Appeals recently upheld a bankruptcy court's determination that the "debtors' pre-bankruptcy application of their right to tax refunds to post-bankruptcy tax obligations constitutes an asset that must be turned over to the bankruptcy trustee," pursuant to § 542.[15] In that case, the debtors applied their 2001 overpayment to their 2002 tax liability, sixteen days prior to filing for bankruptcy relief in 2002. Although the trustee demanded turnover of that pre-payment, the debtors did not comply. In 2003, the debtors filed their 2002 tax return, applying the pre-payment to their tax liability. The trustee sought turnover of the pre-payment from the debtors, who responded that their pre-payment election had "extinguished their interest" in those funds, leaving nothing for the trustee to claim on behalf of the estate. The court disagreed, stating that "nothing in section 541 [defining estate property] requires that the debtor's interest be

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[14] *Id.* at 778-79.

[15] *Nichols v. Birdsell*, 491 F.3d 987, 988 (9th Cir. 2007).

immediately capable of being liquidated into cash in order to constitute property of the estate."[16] As such, the court held that the debtors' right to a "credit toward future taxes constituted estate property at the time the Debtors filed for bankruptcy."[17]

Significantly, the *Nichols* court focused entirely on the issue of whether or not the pre-payment was property of the estate, rather than the issue of whether turnover was an appropriate remedy, and is therefore distinguishable. In the present matter, the propriety of turnover is the exclusive issue. Assuming, without deciding, that the pre-payment constitutes estate property as a contingent reversionary interest, this Court must decide whether the Bankruptcy Code empowers trustees to demand its turnover. We hold that it does not. Turnover is a remedy that is specifically limited by § 542 to "property that the trustee may use, sell, or lease," and is in the turnover target's possession or control during the bankruptcy case. A contingent reversionary interest in funds held by another is simply not something that is in the debtor's possession that can be turned over to the trustee. Even if a debtor had an equivalent amount of funds in an accessible account, a trustee could not compel their turnover unless he could prove that those funds were the proceeds of the pre-payment. A trustee in bankruptcy can no more compel

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[16] *Id.* at 990.

[17] *Id.*

a debtor to turnover funds that he does not have than he can squeeze blood out of a turnip.[18]

The Bankruptcy Code does not expand the debtor's interests against others, "and, if those interests were limited [when the petition was filed], the trustee's rights to possession are similarly limited."[19] When the petition was filed in this case, the Debtors had no current right to possession of the pre-paid taxes. This is equally true as of the time that the Trustee filed the adversary proceeding from which this appeal arose. A contingent right to a refund in the event that the Debtors overpaid their 2007 taxes is not something, in our opinion, that is subject to turnover. Simply put, under these facts, the Trustee may not take that which the Debtors do not have. For this Court to hold otherwise could allow trustees to compel pre-petition tax withholdings by debtors' employers to be subject to turnover actions against the debtors, since such payments may also be deemed tax "credits." However, such is not the purpose or the effect of the turnover power.

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[18] Nonetheless, we specifically decline to make any determination here regarding the propriety of a turnover request directed at a debtor who leaves himself without the ability to comply with a turnover request by inappropriately dissipating estate property post-petition.

[19] *Grant v. United States (In re Simmons)*, 124 B.R. 606, 607 (Bankr. M.D. Fla. 1991) (citing 4 *Collier on Bankruptcy* ¶ 541.01, at 541-5, 54-7 (15th ed. 1979)).

We need not, and do not, decide the more difficult issue of the estate's interest in the prepaid funds, nor whether the Trustee has any currently cognizable claim against the IRS for return of any of the prepaid funds.[20] Our decision is limited to the propriety of turnover under the facts of the present case.

V. CONCLUSION

Since the funds sought by the Trustee were not within the Debtors' possession, custody, or control during the pendency of the bankruptcy case, we hold that the bankruptcy court properly refused to order turnover of the pre-paid taxes. The bankruptcy court's judgment is therefore affirmed.

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[20] In fact, the appellate record does not indicate the current status of Debtor's tax liability. By now, Debtor most likely has filed his 2007 tax return, and his 2007 tax liability has been established. Though he may well have received a refund from the IRS, that refund was not at issue in the case before this Court, and we do not opine as to the parties' respective entitlement to any such funds.

IN RE JAMES WINSLOW GRAVES, doing business as Custom Woods Construction, LLC, and KATHRYN PATRICIA GRAVES, Debtors. JEFFREY A. WEINMAN, Trustee, Appellant, v. JAMES WINSLOW GRAVES and KATHRYN PATRICIA GRAVES, Appellees.

BAP No. CO-08-038

UNITED STATES BANKRUPTCY APPELLATE PANEL FOR THE TENTH CIRCUIT

396 B.R. 70; 2008 Bankr. LEXIS 2641; Bankr. L. Rep. (CCH) P81,344; 102 A.F.T.R.2d (RIA) 6762

October 22, 2008, Filed

COUNSEL: Submitted on the briefs:* Jeffrey A. Weinman, Trustee, Pro se.

JUDGES: Before BOHANON, MICHAEL, and THURMAN, Bankruptcy Judges.

OPINION BY: THURMAN

OPINION

THURMAN, Bankruptcy Judge.

The Chapter 7 bankruptcy trustee appeals the bankruptcy court's order denying his motion to

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* The parties did not request oral argument, and after examining the briefs and appellate record, the Court has determined unanimously that oral argument would not materially assist in the determination of this appeal. *See* Fed. R. Bankr. P. 8012. The case is therefore ordered submitted without oral argument.

compel debtors, James and Kathryn Graves ("Debtors") to turnover the value of a pre-petition tax refund that Debtors applied to pre-payment of their 2007 taxes, prior to filing their bankruptcy case. We affirm.

I. BACKGROUND

In July 2007, Debtors filed their 2006 tax return. Pursuant to that return, Debtors were entitled to a refund for overpayment of taxes in the amount of $ 3,000.[1] The Debtors filed a voluntary Chapter 7 bankruptcy petition on September 20, 2007, and did not elect to split their tax year pursuant to 26 U.S.C. § 1398(d)(2).[2] In January 2008, trustee Jeffrey Weinman ("Trustee"), filed a motion for turnover of the Debtors' 2006 tax refund. The Debtors responded, and the matter was considered at a non-evidentiary hearing on March 26, 2008. The bankruptcy court ruled orally on the record and, on the same date, issued a minute entry denying the Trustee's motion.

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[1] Although the Debtors' tax return directs that the amount of $ 3,820 be applied to their 2007 estimated tax, this is because they failed to subtract the amount of taxes owed for 2006, $ 820, from the amount of taxes paid in 2006, $ 3,820. *See* Debtors' IRS 1040 (2006) at 2, in Appellants' Amended Appendix at 19. Thus, their actual refund entitlement was only $ 3,000, and that is the amount for which they received a pre-payment credit.

[2] This provision allows debtors in Chapter 7 and 11 cases to treat their taxable year as two taxable years; one ending on the day prior to filing of their petition, and the other beginning on the petition date. However, any such election must be made on or prior to the date on which the bankruptcy case is commenced.

The Trustee filed a notice of appeal on April 4, 2008 and, on June 3, 2008, this Court issued an order determining the minute entry to be a final order for the purposes of appeal.

II. APPELLATE JURISDICTION

This Court has jurisdiction to hear timely-filed appeals from final judgments and orders of bankruptcy courts within the Tenth Circuit, unless one of the parties elects to have the district court hear the appeal.[3] Because this Court has already determined that the order sought to be appealed is final, the notice of appeal was timely filed, and no party to this appeal has elected to have the appeal heard by the district court, this Court has appellate jurisdiction.

III. ISSUE AND STANDARD OF REVIEW

The single issue presented by this appeal is whether a pre-petition tax refund that the Debtors elected to apply in pre-payment of a subsequent year's tax liability is properly subject to turnover pursuant to 11 U.S.C. § 542. This is an issue of law, which this Court reviews *de novo*.[4]

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[3] 28 U.S.C. § 158(a)(1), (b)(1), and (c)(1); Fed. R. Bankr. P. 8002.

[4] *In re Duncan*, 329 F.3d 1195, 1198 (10th Cir. 2003).

IV. DISCUSSION

This appeal exemplifies the concept that "you cannot get blood out of a turnip." The Trustee seeks to obtain from the Debtors that which they simply do not have: the amount they could have received from the IRS in 2007, but did not. In most lawsuits or contested matters, plaintiffs or others obtain judgments or orders for damages without consideration of the defendants' ability to pay. However, this is not an ordinary matter, but a Chapter 7 bankruptcy case, which is governed by the Bankruptcy Code. Thus, in this case, a trustee has been appointed to, among other duties, "collect and reduce to money the property of the estate."[5] In order to carry out their duties, bankruptcy trustees are given certain powers by the Bankruptcy Code. Section 542(a) of the Bankruptcy Code authorizes a bankruptcy trustee to compel turnover of estate property from anyone who has it in their "possession, custody, or control, during the case."[6] The Trustee contends that the Debtors' 2006 tax refund is both property of the estate and subject to the turnover power. The Debtors respond that, because of their pre-payment election, they are not now, and never have been, in possession, custody, or control of that refund during the pendency of the bankruptcy case.

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[5] 11 U.S.C. § 704(a).

[6] 11 U.S.C. § 542(a).

This is not the first case involving such a dispute. Several of these cases deserve our analysis. In 1948, the United States Supreme Court defined the pre-Bankruptcy Code turnover power, noting that "the primary condition of [turnover] relief is possession of existing chattels or their proceeds capable of being surrendered by the person ordered to do so."[7] The Court also noted that "we do not consider resort to this particular proceeding [turnover] appropriate if, at the time it is instituted, the property and its proceeds have already been dissipated, no matter when that dissipation occurred."[8] These concepts were subsequently incorporated into the statutory turnover provision, § 542(a).

In *Grant v. United States* (*In re Simmons*),[9] the debtor elected to have an overpayment of taxes applied to his next year's tax liability. Six days later, he filed for Chapter 7 bankruptcy relief. The trustee in bankruptcy filed an adversary proceeding against the Internal Revenue Service ("IRS") seeking turnover of the prepaid funds. The court denied the relief, finding that the prepaid funds were not property of the estate, stating:

> Thus, debtor's overpayment, at his election, became a payment of his 1988 estimated tax

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[7] *Maggio v. Zeitz* (*In re Luma Camera Serv., Inc.*), 333 U.S. 56, 64, 68 S. Ct. 401, 92 L. Ed. 476 (1948).

[8] *Id.* at 64.

[9] 124 B.R. 606 (Bankr. M.D. Fla. 1991).

> rather than an overpayment of his 1987 taxes. Once debtor made this election, as a matter of law, he no longer had an overpayment for which he could file a claim for refund. Consequently, the debtor's prepetition estimated tax payment cannot be considered a legal or equitable interest of the debtor in property as of the commencement of the case, and such payment is not subject to turnover.

Id., at 607-08. This outcome was based, in part, on the Internal Revenue Code, 26 U.S.C. § 6513(d), which provides that, where an overpayment of tax is applied as a credit on the next year's taxes, "no claim for refund of such overpayment shall be allowed for the taxable year in which the overpayment arises."

The trustee in *Wittman v. United States* (*In re Weir*),[10] similarly attempted to obtain prepaid taxes from the IRS, asserting claims for turnover, voidable preference, and fraudulent conveyance. The court rejected all three claims. With respect to the turnover claim, the court noted that, once the prepayment election had been made, "debtor retained only the right to have the payment credited against his 1985 tax liability and to have any excess refunded to him."[11] However, the court did note that, although the estate was not entitled to recover the prepayments as

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[10] No. 85-40456-7, 1990 Bankr. LEXIS 778, 1990 WL 63072 (Bankr. D. Kan. Apr. 3, 1990).

[11] 1990 Bankr. LEXIS 778, [WL] at *2.

property of the estate, it "would be entitled to share in any refund due the debtor."[12]

In *In re Middendorf,*[13] debtors pre-paid $ 22,250 on their 2005 taxes, eight days before filing a Chapter 7 petition. In 2006, debtors filed their 2005 tax return, which entitled them to a refund in excess of $ 20,000. The trustee made demand on the IRS for the entire pre-payment amount, contending that it was a preferential transfer. Trustee and the IRS entered a settlement, subject to the court's approval, for turnover of the entire pre-payment amount. Debtors objected. The court found that the debtors' pre-payment did not constitute a preference, because a preference requires proof of payment of an antecedent debt. Since debtors' 2005 tax obligation did not arise until the end of 2005, and the prepayment occurred in April 2005, the trustee could not prove that element of the claim. Likewise, the court held that the pre-payment was not a fraudulent transfer because debtors had received reasonably equivalent value for the payment, which consisted of a dollar for dollar credit and the right to a refund if their next year's tax debt was less than the pre-payment. Nonetheless, the court held that "the portion of Debtors' tax refund attributable to pre-petition withholdings and payments is Estate property," and that the

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[12] *Id.*

[13] 381 B.R. 774 (Bankr. D. Kan. 2008).

debtors' "contingent reversionary interest" vests "once the ultimate tax liability is assessed and satisfied."[14]

Finally, the Ninth Circuit Court of Appeals recently upheld a bankruptcy court's determination that the "debtors' pre-bankruptcy application of their right to tax refunds to post-bankruptcy tax obligations constitutes an asset that must be turned over to the bankruptcy trustee," pursuant to § 542.[15] In that case, the debtors applied their 2001 overpayment to their 2002 tax liability, sixteen days prior to filing for bankruptcy relief in 2002. Although the trustee demanded turnover of that pre-payment, the debtors did not comply. In 2003, the debtors filed their 2002 tax return, applying the pre-payment to their tax liability. The trustee sought turnover of the pre-payment from the debtors, who responded that their pre-payment election had "extinguished their interest" in those funds, leaving nothing for the trustee to claim on behalf of the estate. The court disagreed, stating that "nothing in section 541 [defining estate property] requires that the debtor's interest be immediately capable of being liquidated into cash in order to constitute property of the estate."[16] As such, the court held that the debtors' right to a "credit

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[14] *Id.* at 778-79.

[15] *Nichols v. Birdsell*, 491 F.3d 987, 988 (9th Cir. 2007).

[16] *Id.* at 990.

toward future taxes constituted estate property at the time the Debtors filed for bankruptcy."[17]

Significantly, the *Nichols* court focused entirely on the issue of whether or not the pre-payment was property of the estate, rather than the issue of whether turnover was an appropriate remedy, and is therefore distinguishable. In the present matter, the propriety of turnover is the exclusive issue. Assuming, without deciding, that the pre-payment constitutes estate property as a contingent reversionary interest, this Court must decide whether the Bankruptcy Code empowers trustees to demand its turnover. We hold that it does not. Turnover is a remedy that is specifically limited by § 542 to "property that the trustee may use, sell, or lease," and is in the turnover target's possession or control during the bankruptcy case. A contingent reversionary interest in funds held by another is simply not something that is in the debtor's possession that can be turned over to the trustee. Even if a debtor had an equivalent amount of funds in an accessible account, a trustee could not compel their turnover unless he could prove that those funds were the proceeds of the pre-payment. A trustee in bankruptcy can no more compel a debtor to turnover funds that he does not have than he can squeeze blood out of a turnip.[18]

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[17] *Id.*

[18] Nonetheless, we specifically decline to make any determination here regarding the propriety of a turnover request

(Continued on following page)

The Bankruptcy Code does not expand the debtor's interests against others, "and, if those interests were limited [when the petition was filed], the trustee's rights to possession are similarly limited."[19] When the petition was filed in this case, the Debtors had no current right to possession of the pre-paid taxes. This is equally true as of the time that the Trustee filed the adversary proceeding from which this appeal arose. A contingent right to a refund in the event that the Debtors overpaid their 2007 taxes is not something, in our opinion, that is subject to turnover. Simply put, under these facts, the Trustee may not take that which the Debtors do not have. For this Court to hold otherwise could allow trustees to compel pre-petition tax withholdings by debtors' employers to be subject to turnover actions against the debtors, since such payments may also be deemed tax "credits." However, such is not the purpose or the effect of the turnover power.

We need not, and do not, decide the more difficult issue of the estate's interest in the prepaid funds, nor whether the Trustee has any currently cognizable claim against the IRS for return of any of the prepaid

---

directed at a debtor who leaves himself without the ability to comply with a turnover request by inappropriately dissipating estate property post-petition.

[19] *Grant v. United States* (*In re Simmons*), 124 B.R. 606, 607 (Bankr. M.D. Fla. 1991) (citing 4 Collier on Bankruptcy P 541.01, at 541-5, 541-7 (15th ed. 1979)).

funds.[20] Our decision is limited to the propriety of turnover under the facts of the present case.

V. CONCLUSION

Since the funds sought by the Trustee were not within the Debtors' possession, custody, or control during the pendency of the bankruptcy case, we hold that the bankruptcy court properly refused to order [] turnover of the pre-paid taxes. The bankruptcy court's judgment is therefore affirmed.

---

[20] In fact, the appellate record does not indicate the current status of Debtor's tax liability. By now, Debtor most likely has filed his 2007 tax return, and his 2007 tax liability has been established. Though he may well have received a refund from the IRS, that refund was not at issue in the case before this Court, and we do not opine as to the parties' respective entitlement to any such funds.

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLORADO IN BANKRUPTCY

Minutes of Proceeding/Minute Order

Date: March 26, 2008
Honorable A. Bruce Campbell, Presiding

In re: James and Kathryn Graves
Case No. 07-20569 ABC
Chapter 7

Debtors.

Appearances

	Chapter 7 Trustee		
Trustee	Jeffrey A. Weinman	Counsel	Pro Se
Debtors		Counsel	Anne E. DeWitt

Proceedings: Trustee's Motion for Turnover of Property of the Estate of Debtors' Response thereto

[ ] Witnesses sworn [ ] See attached list
[ ] Exhibits entered [ ] See attached list

[ ]

Orders:

[x] Relief sought in complaint/motion:

[ ] Granted [x] Denied*

[ ] Dismissed [ ] Awarded by default

[ ] Judgment to enter for:

[ ] Plaintiff [ ] Defendant

[ ] Applicant [ ] Respondent

[ ] in the amount of $ _____

[ ] Matter taken under advisement

[x] Oral findings and conclusions made of record

[ ] Formal order or judgment to enter

[ ] Continued to _____

* denied without prejudice

Date: March 26, 2008 FOR THE COURT:
Bradford L. Bolton, Clerk

By: /s/ [Illegible]

IT IS SO ORDERED

/s/ A. Bruce Campbell
Judge A. Bruce Campbell

JAMES NICHOLS; BEVERLY ANN NICHOLS, Plaintiffs-Appellants, v. DAVID A. BIRDSELL, Defendant-Appellee.

No. 05-15554

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

491 F.3d 987; 2007 U.S. App. LEXIS 10919; Bankr. L. Rep. (CCH) P80,926; 57 Collier Bankr. Cas. 2d (MB) 1820

February 16, 2007, Argued and Submitted, San Francisco, California
May 9, 2007, Filed

COUNSEL: Michael J. Fatta, Law Office of Michael J. Fatta, PLLC, Glendale, Arizona, for the plaintiffs-appellants.

Terry A. Dake, Terry A. Dake, LTC., Phoenix, Arizona, for the defendant-appellee.

JUDGES: Before: J. Clifford Wallace, Richard D. Cudahy,* and M. Margaret McKeown, Circuit Judges.

OPINION BY: J. Clifford Wallace

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* The Honorable Richard D. Cudahy, Senior United States Circuit Judge for the Seventh Circuit, sitting by designation.

OPINION

WALLACE, Senior Circuit Judge:

This case presents a new issue for our court: whether debtors' pre-bankruptcy application of their right to tax refunds to post-bankruptcy tax obligations constitutes an asset that must be turned over to the bankruptcy trustee pursuant to the Bankruptcy Code, 11 U.S.C. § 542. Plaintiffs-Appellants James W. Nichols and Beverly Nichols (Debtors) appeal from the district court's order denying their appeal from the bankruptcy court decision. In the underlying case, the bankruptcy court concluded that the pre-petition application of the right to the tax refund was an asset as of the petition date, and that the Debtors must therefore deliver to the trustee the value of the property under section 542(a). We agree, and affirm the district court's order denying the Debtors' appeal.

I.

David A. Birdsell, the trustee of the Debtors' bankruptcy estate (Trustee), filed an amended complaint in the United States Bankruptcy Court alleging a claim in the Debtors' interest in tax overpayments. The facts are not in dispute. The Debtors overpaid their 2001 federal and state income tax returns and were entitled to tax refunds as a result of the overpayments. Rather than obtain a current refund of that money, the debtors elected to leave those funds on deposit with the United States and the State of Arizona, respectively, and apply the

overpayments to their future tax liability. Sixteen days later, on February 5, 2002, the Debtors filed for bankruptcy. The Trustee demanded that the Debtors turn the deposits over to the Trustee, but this was not done. In February of 2003, the Debtors signed their 2002 federal and state income tax returns and applied the deposits (resulting from the overpayment of their 2001 taxes) to their 2002 tax liabilities.

The Trustee moved for partial summary judgment on the amended complaint, arguing that the Debtors' interest in the tax overpayments was property of the bankruptcy estate pursuant to 11 U.S.C. § 541 that must be turned over to the Trustee under section 542. The Debtors opposed the motion and also moved for summary judgment. The Debtors observed that, after making the election, they were no longer entitled to a tax refund. They contended that the election to apply the deposits to future tax liabilities extinguished their interest in the tax refund and left no property interest for the bankruptcy estate.

The bankruptcy court granted the Trustee's motion for summary judgment, concluding that the Debtors' prepayment of their tax liability constituted an asset of the estate as of the petition date, and that the Debtors must deliver to the Trustee the value of that asset under section 542(a). The Debtors appealed to the district court, and the district court denied the appeal.

On appeal to this court, the Debtors argue that their prebankruptcy application of their tax overpayment to the subsequent year's tax obligation was not property of their bankruptcy estate. They observe that Internal Revenue Code §§ 6402(b) and 6513(d) provide for a taxpayer to make an irrevocable election applying an overpayment of taxes to the subsequent year's tax obligation. They further contend that the election changed the character of the overpayment to a payment of estimated taxes, leaving no interest for the bankruptcy estate.

We have jurisdiction under 28 U.S.C. § 1291, and review de novo the district court's decision on an appeal from a bankruptcy court. *See In re Bankr. Estate of MarkAir, Inc.*, 308 F.3d 1057, 1059 (9th Cir. 2002). The bankruptcy court's conclusions of law are reviewed de novo, and its factual findings for clear error. *Id.* We review de novo questions of statutory construction. *See id.*

II.

Section 542 provides in part,

> Except as provided in subsection (c) or (d) of this section, an entity, other than a custodian, in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease under section 363 of this title, or that the debtor may exempt under section 522 of this title, shall deliver to the trustee, and account for, such property or the value of such property, unless such

> property is of inconsequential value or benefit to the estate.

11 U.S.C. § 542(a). Section 541 defines property as "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1).

In *In re Feiler*, 218 F.3d 948 (9th Cir. 2000), we addressed an analogous issue under the Bankruptcy Code. The Feilers had net operating losses (NOLs) in 1993. *Id.* at 950. Under the tax code at that time, they had two options: (1) carry back the NOLs and apply them to the past three taxable years, carrying forward any remainder; or (2) waive the carryback provision and carry forward the entire NOLs. *Id.* at 950-51. Under the first option, applying the NOLs to the past years would result in a current tax refund to the debtors. Carrying forward the NOLs under the second option could result in a reduction of tax liability in future years, since the NOLs could be used to offset future income.

The Feilers chose the second option, to waive the carryback. *Id.* at 951. Had they chosen the first option, they would have been entitled to a tax refund of over $ 280,000. *Id.* The following year, five months after making the election, the Feilers declared bankruptcy. *Id.* The bankruptcy trustee filed income requests for the tax refund that the Feilers would have received had they chosen the first option. *Id.* The Internal Revenue Service (IRS) disallowed the refund on the grounds that the Feilers had made an

irrevocable election to carry forward the NOLs. *Id.* The trustee filed suit against the government, seeking to set aside the Feilers' previous election under section 548, a code section that involves fraudulent transfers. *Id.* The bankruptcy court granted summary judgment in favor of the bankruptcy trustee, and we affirmed. *Id.*

Feiler is different from this case in that it involved an election relating to NOLs, and not a prepayment of taxes. *Id.* at 950. In addition, the issue in *Feiler* was whether the debtors' irrevocable election should be set aside under section 548, not section 542. *Id.* at 951. Under section 548, the trustee may avoid certain fraudulent transfers of an "interest of the debtor in property" that were "made or incurred on or within 2 years before the date of the filing of the petition." 11 U.S.C. § 548(a)(1). In contrast, the issue in the instant case is whether the prepayment of taxes constitutes estate property under section 542 at the time of the bankruptcy filing. Thus, *Feiler* is not dispositive.

Our reasoning in *Feiler* is nevertheless instructive. *Feiler* stated that the first issue was whether "the election to forgo a tax refund and waive the carryback on the NOLs involved an interest in property." 218 F.3d at 955 (quotation marks omitted). Interpreting the term "property" broadly, we held that "[b]ecause the right to receive a tax refund constitutes an interest in property, . . . the election to waive the carryback and relinquish the right to a refund necessarily implicates a property interest." *Id.*

We observed that "the Supreme Court has explained that the term property has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed." *Id.* (internal quotation marks omitted) (*citing Segal v. Rochelle*, 382 U.S. 375, 379, 86 S. Ct. 511, 15 L. Ed. 2d 428 (1966)).

The Debtors contend that their inability to get the funds back from the IRS and the irrevocable nature of their election prevents the bankruptcy estate from asserting any right to the funds. However, nothing in section 541 requires that the debtor's interest be immediately capable of being liquidated into cash in order to constitute property of the estate. *See* 11 U.S.C. § 541. Instead, section 541(c)(1) provides that a debtor's interests become property of the estate even in circumstances in which the interest cannot be liquidated and transferred by the debtor. 11 U.S.C. § 541(c)(1); *cf. In re O'Gorman-Sykes*, 245 B.R. 815, 819 (Bankr. E.D. Va. 1999) (holding that anticipated tax refunds are property of the bankruptcy estate under section 541(a)).

As a result of the election, the Debtors were left with a credit with the IRS that provided a dollar-for-dollar tax reduction in the following year. If the Nichols had not elected to prepay their taxes, those funds would have been refunded to them and would likely have been available for the bankruptcy estate when they voluntarily filed for bankruptcy just 16 days later. The fact that the election, once made, was irrevocable, does not change the analysis. In light of

the expansive definition of property contained in the Bankruptcy Code and our broad interpretation of "property" under *Feiler*, we hold that this credit toward future taxes constituted estate property at the time the Debtors filed for bankruptcy. *Cf. In re Ryerson*, 739 F.2d 1423, 1425 (9th Cir. 1984) ("By including all legal interests without exception, Congress indicated its intention to include all legally recognizable interests although they may be contingent and not subject to possession until some future time").

AFFIRMED.

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

Jeffrey A. Weinman, Chapter 7 Trustee, Appellant Plaintiff/ Petitioner-Appellant, v. James Winslow Graves and Kathryn Patricia Graves Defendant/ Respondent-Appellee.	Case No. 08-1462 **APPELLANT/ PETITIONER'S OPENING BRIEF**

On Appeal from the United States Bankruptcy
Appellate Panel for the Tenth Circuit
BAP Case No. CO-08-038

Respectfully Submitted,

WEINMAN & ASSOCIATES, P.C.

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Oral Argument is not requested.

SCANNED PDF FORMAT ATTACHMENTS ARE INCLUDED WITH DIGITAL SUBMISSION SENT VIA EMAIL

Dated: February 6, 2009

TABLE OF CONTENTS

TABLE OF AUTHORITIES 3

PRIOR OR RELATED APPEALS 4

STATEMENT OF JURISDICTION 4

STATEMENT OF THE ISSUES 5

STATEMENT OF THE CASE 5

STATEMENT OF THE FACTS 6

SUMMARY OF THE ARGUMENTS 9

IS THE CREDIT CREATED BY THE APPLICATION OF THE GRAVES' 2006 TAX REFUND TO THEIR SUBSEQUENT TAX LIABILITY FOR 2007 PROPERTY OF THEIR BANKRUPTCY ESTATE 10

IS A MOTION FOR TURNOVER OF PROPERTY OF THE ESTATE THE PROPER METHOD FOR THE TRUSTEE TO PURSUE TO OBTAIN THE GRAVES' TAX CREDIT HELD BY THE IRS FOR THE BANKRUPTCY ESTATE 11

DID THE BANKRUPTCY COURT ERR AS A MATTER OF LAW IN DISMISSING THE TRUSTEE'S MOTION FOR TURNOVER OF THE CREDIT OF THE GRAVES' 2006 FEDERAL TAX REFUND 13

STATEMENT OF COUNSEL AS TO ORAL ARGUMENT..... 13

CONCLUSION..... 13

Certificate of Compliance 15

CERTIFICATE OF DIGITAL SUBMISSION 16

CERTIFICATE OF SERVICE..... 17

TABLE OF AUTHORITIES

CASES

Maggio v. Zeitz (In re Luma Camera Services, Inc.), 68 S.Ct. 401 (1948) 11

In re Nichols, 309 B.R. 41, 45 (Bankr.D.AZ 2004), affirmed, 491 F.3d 987 (9th Cir. 2007) 10, 11, 13

Nichols v. Birdsell, 491 F.3d 987, 990 (9th Cir. 2007) 10, 11

In re Pyatt, 486 F.3d 423 (8th Cir. 2007) 11

Segal v. Rochelle, 86 S.Ct. 511 (1966) 11

STATUTES

11 U.S.C. §541..... 11, 12

11 U.S.C. §541(c)..... 10

11 U.S.C. §541(c)(1) 11, 12, 14

11 U.S.C. §542 13
11 U.S.C. §542(a) 9, 11, 12, 13
28 U.S.C. §158(a)(1) 4
28 U.S.C. §158(b)(1) 4
28 U.S.C. §158(c)(1) 4
28 U.S.C. §158(d)(1) 5
28 U.S.C. §1334 4

OTHER

Rule 4(b)(1) F.R.A.P 5
Rule 8002 F.R.B.P 5

PRIOR OR RELATED APPEALS

United States Bankruptcy Appellate Panel for the Tenth Circuit, *In re James Winslow Graves, d/b/a Custom Woods Construction, LLC and Kathryn Patricia Graves, Debtors,* Bankruptcy Case No. 07-20569 ABC, Chapter 7, Jeffrey A. Weinman, Appellant v. James Winslow Graves and Kathryn Patricia Graves, Appellees, BAP Case No. CO-08-038.

Jeffrey A. Weinman, Chapter 7 Trustee of the bankruptcy estate of James Winslow Graves and Kathryn Patricia Graves, Appellant, for his opening brief states:

STATEMENT OF JURISDICTION

A. UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF COLORADO.

The United States Bankruptcy Court for the District of Colorado has jurisdiction over this matter pursuant to 28 U.S.C. §1334. Mr. and Mrs. Graves ("the Graves") filed their voluntary Chapter 7 bankruptcy petition with the U.S. Bankruptcy Court on September 20, 2007, Bankruptcy Case No. 07-20569 ABC.

B. UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE TENTH CIRCUIT.

The United States Bankruptcy Appellate Panel of the Tenth Circuit had jurisdiction over the appeal from the U.S. Bankruptcy Court for the District of Colorado pursuant to the provisions of 28 U.S.C. §§158(a)(1), (b)(1), and (c)(1); Fed.R.Bankr.P. 8002.

C. UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT.

The Notice of Appeal from the U.S. Bankruptcy Appellate Panel of the Tenth Circuit was timely filed in accordance with Rule 4(b)(1), F.R.A.P. on November 21, 2008. This appellate court's jurisdiction derives from 28 U.S.C. §158(d)(1).

STATEMENT OF THE ISSUES

IS THE CREDIT CREATED BY THE APPLICATION OF THE GRAVES' 2006 TAX REFUND TO THEIR SUBSEQUENT TAX LIABILITY FOR 2007 PROPERTY OF THEIR BANKRUPTCY ESTATE.

IS A MOTION FOR TURNOVER OF PROPERTY OF THE ESTATE THE PROPER METHOD FOR THE TRUSTEE TO PURSUE TO OBTAIN THE GRAVES' TAX CREDIT HELD BY THE IRS FOR THE BANKRUPTCY ESTATE.

DID THE BANKRUPTCY COURT ERR AS A MATTER OF LAW IN DISMISSING THE TRUSTEE'S MOTION FOR TURNOVER OF THE CREDIT OF THE GRAVES' 2006 FEDERAL TAX REFUND.

STATEMENT OF THE CASE

A. BANKRUPTCY COURT

This case is a turnover action brought by the Chapter 7 Trustee demanding turnover of a credit which the Graves had with the IRS with respect to the Graves' 2006 federal tax refund. Pre-petition, the Graves applied their 2006 federal tax refund to their 2007 tax liability resulting in a credit with the Internal Revenue Service. The 2006 tax refund had not been applied by the IRS to the Graves 2007 tax liability at the time they filed their bankruptcy case. On January 21, 2008, the Trustee filed his "Trustee's Motion for Turnover of Property of the Estate". The Graves timely file [sic] a "Response" to the Appellant's Motion for Turnover. The Bankruptcy Court set a non-evidentiary hearing on the Motion for Turnover

and the Response thereto for March 26, 2008. At the hearing, the Bankruptcy Court denied, as a matter of law, the Trustee's Motion for Turnover, holding that the Graves had to have had possession of their 2006 tax refund in order for the Motion for Turnover to be appropriate.

B. UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE TENTH CIRCUIT.

The Bankruptcy Court's Order denying the Trustee's Motion for Turnover was timely appealed to the United States Bankruptcy Appellate Panel of the Tenth Circuit which affirmed the Bankruptcy Court's denial of the Trustee's Motion for Turnover.

STATEMENT OF THE FACTS

A. BACKGROUND.

Appellees, James Winslow Graves and Kathryn Patricia Graves ("the Graves") filed their voluntary Chapter 7 bankruptcy petition with the U.S. Bankruptcy Court for the District of Colorado on September 20, 2007. The Bankruptcy Court Case Number is 07-20569 ABC.

The §341 Meeting of Creditors for the Graves' Chapter 7 bankruptcy proceeding was scheduled and held on October 26, 2007. The Appellant, Jeffrey A. Weinman ("Trustee"), was appointed interim trustee and became the acting trustee of the bankruptcy

estate at the conclusion of the §341 Meeting of Creditors on October 26, 2007.

Prior to the filing of their bankruptcy petition, on July 20, 2007, the Graves made an election with the IRS to apply their 2006 tax refund in the ultimate amount of $3,000 to their 2007 federal tax liability. The initial amount of the Graves' refund was indicated to be $3,820.00. With such election, the Graves received a dollar for dollar credit from the IRS from their 2006 refund.

B. BANKRUPTCY COURT.

Following the filing of the bankruptcy petition on January 15, 2008, the Trustee sent a written request to the Graves' counsel, Sharon W. Grossenbach, Esq. concerning the 2006 federal tax refund which the Graves had applied to their 2007 federal tax liability. [A copy of this request is included at Appellant App. at 60.] On January 18, 2008, the Graves, through their counsel, sent a written response to the Trustee indicating that the Graves had made, pre-petition, an election in July 2007 to apply their 2006 tax refund of $3,000.00 to their 2007 tax liability. Further, the Graves indicated that the election was irrevocable and as such, the 2006 tax refund was no longer under their control, and therefore, not property of their bankruptcy estate. [A copy of the written Response is included at Appellant App. at 20.]

On January 21, 2008, the Trustee filed his "Trustee's Motion for Turnover of Property of the Estate".

The Trustee's Motion for Turnover requests an order from the Bankruptcy Court directing the Graves to turnover $3,000.00 to the bankruptcy estate, such amount representing the Graves' 2006 tax refund. In the Trustee's Motion for Turnover, the Trustee asserts that because the Graves received the benefit of the application of the refund, which is essentially an account receivable of the Graves, the Graves should turnover an equivalent amount to the bankruptcy estate. In effect, because the Graves applied their 2006 federal tax refund to reduce their 2007 federal tax liability, they received the value of their 2006 federal tax refund in the form of a credit with the IRS. The Motion for Turnover was accompanied by a Notice of the Trustee's Motion for Turnover of Property of the Estate which established February 11, 2008 as the deadline for the Graves to file a written response to the Motion for Turnover. [Appellant App. at 13, Bankruptcy Court Docket No. 28.]

The Graves timely filed a "Response" to the Trustee's Motion for Turnover. The Graves responded that they had applied their 2006 tax refunds to their 2007 tax liability, that such application was irrevocable, and as indicated above, the 2006 tax refund was no longer property of their bankruptcy estate. As such, the Graves asserted that they were not required to turnover their 2006 refund to the Trustee. [Appellant App. at 20, Bankruptcy Court Docket No. 29.]

The Bankruptcy Court set a non-evidentiary hearing on the Motion for Turnover and the Response thereto for March 26, 2008.

At the non-evidentiary hearing, the Bankruptcy Court denied the Motion for Turnover. The Minute Order entered on the Bankruptcy Court's docket indicates that the Motion for Turnover was denied "without prejudice". At the hearing, the Court made oral findings and conclusions which were made of record. [Appellant App. at 49, Bankruptcy Court Docket No. 34.] The transcript of the hearing is included in the record of this Appeal. [Appellant App. at 31.]

At the March 26, 2008 hearing, the Bankruptcy Court ruled as a matter of law that a turnover motion for the relief requested by the Trustee was improper. The Bankruptcy Court concluded that the Graves have to physically have something, i.e., something tangible, before the Bankruptcy Court would order a turnover. [Appellant App. at 31, Transcript Page 7, Lines 23 and 24.] The Bankruptcy Court determined that the Graves had to have their 2006 tax refund in their possession. The Bankruptcy Court failed to distinguish between the Graves' 2006 tax refund and the credit that was created by the application of their 2006 tax refund to their 2007 tax liability. The Bankruptcy Court determined that if the Graves did not have the 2006 refund in their possession, then a motion for turnover would invite a contempt proceeding where the defense would be impossibility [sic], which, in the Bankruptcy Court's view, would be a waste of the Bankruptcy Court's time. [Appellant App. at 31, Transcript, Page 10, Lines 10 through 23.] The Bankruptcy Court was clear that if the Graves did not

physically have their 2006 refund, then the Trustee was in the "wrong place" and the Trustee had to pursue some other course of action. [Appellant App. at 31, Transcript, Page 12, Lines 4 through 6.]

C. UNITED STATES BANKRUPTCY APPELLATE PANEL OF THE TENTH CIRCUIT.

The Trustee timely appealed the Bankruptcy Court's decision to the U.S. Bankruptcy Appellate Panel of the Tenth Circuit ("Appellant Panel"). On appeal to the Appellate panel, the Trustee raised three (3) issues. The Appellate Panel affirmed the Bankruptcy Court's ruling that the Graves had to have their 2006 refund in order for the Trustee's Motion for Turnover to be appropriate. Like the Bankruptcy Court, the Appellate Panel failed to distinguish between the Graves' 2006 tax refund and the credit established for the Graves with the IRS as a result of their election to apply their 2006 tax refund to their 2007 tax liability.

SUMMARY OF THE ARGUMENTS

The credit with the IRS which the Graves realized when they elected to apply their 2006 tax refund to their 2007 tax liability was property of their bankruptcy estate. The Bankruptcy Court erred in dismissing the Trustee's Motion for Turnover because it failed to distinguish between such tax credit and the Graves' 2006 refund.

In determining that the Graves had to have their 2006 tax refund in their possession, before turnover was appropriate, the Court ignored the provisions of 11 U.S.C. §541(c) and 11 U.S.C. §542(a).

IS THE CREDIT CREATED BY THE APPLICATION OF THE GRAVES' 2006 TAX REFUND TO THEIR SUBSEQUENT TAX LIABILITY FOR 2007 PROPERTY OF THEIR BANKRUPTCY ESTATE.

Review is De Novo.

The first issue to address is whether the credit that the Graves had with the IRS was property of their bankruptcy estate. The concept of property of the estate is extremely broad and includes all legal or equitable interests of the Graves in property as of the commencement of their case wherever such property is located and by whomever held. 11 U.S.C. §541. The credit which the Graves received from the IRS when they applied their 2006 tax refund to their 2007 tax liability is property of their bankruptcy estate. *Nichols v. Birdsell,* 491 F.3d 987, 990 (9th Cir. 2007).

Nothing in §541 (11 U.S.C. §541) requires the Graves' interest in estate property to be immediately capable of being liquidated into cash in order to constitute property of their bankruptcy estate. 11 U.S.C. §541(c)(1) specifically provides that such interest becomes property of the estate even though such interest cannot be liquidated and transferred by a debtor under applicable non-bankruptcy law. A debtor's interest in property is not outside of estate

property simply because it is novel or contingent or because enjoyment must be postponed. *In re Nichols,* 309 B.R. 41, 45 (Bankr.D.AZ 2004), affirmed, 491 F.3d 987 (9th Cir.) quoting *Segal v. Rochelle,* 86 S.Ct. 511 (1966).

It is not disputed that the Graves elected to apply their 2006 federal tax refund to their 2007 federal tax liability. This election created a credit that the Graves held with the IRS and the value of such credit was in the Graves' possession at the time of the filing of their Chapter 7 bankruptcy proceeding in September 2007. At the time of the filing of their Chapter 7 bankruptcy petition, the Graves did not owe the IRS for their 2007 taxes. Their 2007 taxes would not be due until 2008. The Graves received a credit that would either reduce their 2007 tax liability, or if there was no 2007 tax liability, would result in the Graves receiving a refund. The credit, although not immediately realizable by the Graves on the date they filed their bankruptcy petition, was an asset which belonged to the Graves that would ultimately realize for the Graves a dollar-for-dollar benefit at the end of 2007 when their 2007 tax liability to the IRS (if any) became due. The credit that the Graves established with the IRS was an asset of their bankruptcy estate that was ultimately realizable by them either in the form of a refund or in the form of payment of their tax liability for 2007. *In re Nichols,* supra, page 45.

The Graves argument that because of their election to apply their 2006 tax refund to their potential 2007 tax liability was irrevocable and therefore

not property of the estate, clearly ignores the provisions of 11 U.S.C. §541(c)(1). *Nichols v. Birdsell*, supra, Page 990 ("nothing in section 541 requires that the debtor's interest be immediately capable of being liquidated into cash in order to constitute property of the estate").

By electing to apply their 2006 tax refund to their 2007 tax liability, the Graves enjoyed the benefit and value of their 2006 tax refund at the time of the filing of their petition and that such value therefore constitutes property of their estate pursuant to 11 U.S.C. §541.

A MOTION FOR TURNOVER OF PROPERTY OF THE ESTATE IS THE PROPER METHOD FOR A CHAPTER 7 BANKRUPTCY TRUSTEE TO PURSUE TO OBTAIN THE DEBTOR'S TAX CREDIT FOR THE BANKRUPTCY ESTATE.

Review is *De Novo*.

The issuance of a turnover order by a Bankruptcy Court is appropriate when the evidence satisfactorily establishes the existence of the property or its proceeds and possession thereof by the debtor during the bankruptcy proceeding. 11 U.S.C. §542(a), *Maggio v. Zeitz (In re Luma Camera Services, Inc.)*, 68 S.Ct. 401 (1948). By authorizing a turnover proceeding against a debtor who has control of property or its proceeds, the bankruptcy trustee is allowed to recover the liquidated value of the property. *In re Pyatt*, 486 F.3d 423 (8th Cir. 2007). In both pre-Code practice and

current law, if a debtor transfers property of the estate and receives value for it, a trustee may compel him to turnover the value of the property because he still has control over the proceeds of, or alternatively the value of the property unless such value is inconsequential. 11 U.S.C. §542(a).

Because the Graves elected to apply their 2006 tax refund to their potential 2007 tax liability, they were left with a credit with the IRS that would provide a dollar for dollar tax reduction in the amount of $3,000.00 for any tax liability in 2007. Such credit provided the Graves with value, either reducing their 2007 tax liability, or alternatively, if no such tax liability existed, then a refund. If the Graves had not made their election, their 2006 refund would have been returned to them. Given the time of the filing of their 2006 tax return (July 2007) and the date of the filing of their Chapter 7 bankruptcy petition (September 20, 2007), it is highly unlikely that the Debtors would have received such refund prior to the date of the filing of their bankruptcy petition. Under the circumstances of this matter, the Graves enjoyed the value of their 2006 tax refund. Such value was in their possession during the pendency of their bankruptcy case. The Trustee's Motion for Turnover was appropriate and should not have been dismissed by the Bankruptcy Court.

THE BANKRUPTCY COURT ERRED (AS A MATTER OF LAW) IN DISMISSING THE TRUSTEE'S MOTION FOR TURNOVER OF THE VALUE OF THE GRAVES' 2006 FEDERAL TAX REFUND.

Review is *De Novo.*

Under the circumstances of this case, the Bankruptcy Court erred as a matter of law in dismissing the Trustee's Motion for Turnover of the value of the Graves' 2006 federal tax refund. In determining that the Graves had to have something physical or tangible, i.e. their actual 2006 tax refund, before it would order turnover, the Bankruptcy Court clearly failed to distinguish between the credit which the Graves enjoyed and their refund. The Bankruptcy Court also ignored the provisions of 11 U.S.C. §541(c)(1) and 11 U.S.C. §542. 11 U.S.C. §542(a) is not limited to property that a debtor can transfer in kind to a trustee because 11 U.S.C. §542(a) alternatively requires that "the value of such property" be delivered to the Trustee. *In re Nichols,* supra at 45.

STATEMENT OF COUNSEL AS TO ORAL ARGUMENT

Oral argument is not requested.

CONCLUSION

The Judgment of the United Stated Bankruptcy Appellate Panel of the Tenth Circuit affirming the Bankruptcy Court's Order, and the Bankruptcy

Court's Order denying the Trustee's Motion for Turnover should be reversed and this matter remanded back to the Bankruptcy Court for a determination of his Motion for Turnover of the value of the Graves' 2006 federal tax credit.

DATED: February 6, 2009

Respectfully Submitted,

WEINMAN & ASSOCIATES, P.C.

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